

forward-looking high-cost support mechanism for non-rural carriers so that it could be applied to rural carriers, was a reasonable approach to take in light of the record in the proceeding.²²⁹ In so doing, the Commission and the Joint Board recognized that the plan adopted in the *Rural Task Force Order* was an interim plan.²³⁰

92. The Commission did not adopt the Rural Task Force's specific proposal to freeze per-line high-cost loop support upon competitive entry into a rural carrier study area, concluding that adoption of the proposal was not warranted at that time.²³¹ The stated purpose of this proposal was to prevent excessive growth in the universal service fund as a result of an incumbent carrier's loss of lines to a competitive ETC.²³² While the Commission recognized that excessive growth in the fund might be possible during the life of the five-year plan under certain circumstances, it concluded that the likelihood of excessive fund growth due to an incumbent carrier's loss of lines to a competitive ETC in the immediate future was speculative.²³³ The Commission, however, indicated its intent to closely monitor these matters, consistent with its obligation under section 254 to maintain a specific, predictable, and sufficient universal service fund.²³⁴

B. Discussion

1. Supporting a Single Connection Is Consistent With the 1996 Act

93. We believe that limiting the scope of high-cost support to a single connection to the public telephone network would be more consistent with the goals of section 254 than the present system. Supporting a single connection to the public telephone network fulfills the goal of "reasonably comparable" access in all regions of the Nation.²³⁵ Section 254(b)(3)'s objective is that consumers in rural areas have access to rates and services, including advanced services, that are reasonably comparable to those available in urban areas.²³⁶ Supporting a single connection provides access to all of the services included in the definition of universal service under section 254(c), because each ETC is required to provide all of the supported services.²³⁷ Supporting a single connection also provides access to all of the additional telecommunications and information services, including advanced services, available to consumers through the public telephone network.²³⁸ Thus, supporting multiple connections is not

²²⁹ See *Rural Task Force Order*, 16 FCC Rcd at 11248-49, paras. 8-10.

²³⁰ *Id.* at 11248, para. 8.

²³¹ *Id.* at 11294, para. 123. The proposed per-line cap would have applied to high-cost loop support. *Id.*

²³² *Id.* at 11294, para. 125.

²³³ *Id.* at 11294, 11325-26, paras. 123-24, 207 ("[A]s an incumbent 'loses' lines to a competitive eligible telecommunications carrier, the incumbent must recover its fixed costs from fewer lines, thus increasing its per-line costs. With higher per-line costs, the incumbent would receive greater per-line support, which would also be available to the competitive eligible telecommunications carrier for each of the lines that it serves. Thus, a substantial loss of an incumbent's lines to a competitive eligible telecommunications carrier could result in excessive fund growth.").

²³⁴ *Id.* at 11297-98, para. 131.

²³⁵ 47 U.S.C. § 254(b)(3).

²³⁶ *Id.*; see also *id.* at § 254(b)(2) ("Access to advanced telecommunications and information services should be provided in all regions of the Nation.").

²³⁷ *Id.* at § 254(c); see *id.* at § 214(e)(1)(A).

²³⁸ See *Rural Task Force Order*, 16 FCC Rcd at 11322, para. 200 ("The public switched telephone network is not a single-use network. Modern network infrastructure can provide access not only to voice services, but also to data, graphics, video, and other services."); see also *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities, Universal Service Obligations of Broadband Providers, Computer III Further Remand*

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necessary to achieve reasonably comparable access in rural areas. Supporting a single connection faithfully accomplishes this objective.²³⁹

94. We disagree with commenters who argue that supporting a single point of access is inconsistent with section 254(b)(3) because rates might rise for second lines, which are often used for access to information services such as dial-up Internet access or fax services.²⁴⁰ We recognize, of course, that supporting multiple connections is advantageous to consumers in high-cost areas. Section 254(b)(3) encourages access to connectivity, however, not unlimited connections at supported rates. Advanced services increasingly are being provided along with voice services over a single connection.²⁴¹ Nothing in the Act supports the argument that multiple connections should be supported for access to dial-up Internet access or fax services, neither of which is a supported service. For similar reasons, we disagree with commenters who argue that supporting multiple connections is necessary to ensure reasonably comparable access to wireless service in rural areas.²⁴² Mobility is not a supported service.²⁴³ Deployment of rural wireless infrastructure is an important policy goal,²⁴⁴ but the reasonable comparability principle does not justify supporting multiple connections to achieve it. We emphasize that, under our recommended approach, support would be available for wireless connections to the extent that customers choose to obtain connectivity through primary connections provided by wireless ETCs.

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Proceedings: Bell Operating Company Provision of Enhanced Services; 1998 Biennial Regulatory Review - Review of Computer III and ONA Safeguards and Requirements, Notice of Proposed Rulemaking, CC Docket Nos. 02-33, 95-20, 98-10, 17 FCC Rcd 3019, 3025-26, para. 11 n.19 (2002) ("With the addition of certain electronics to the telephone line, carriers can transform the copper loop that already provides voice service into a conduit for high-speed traffic.").

²³⁹ See *First Recommended Decision*, 12 FCC Rcd at 132-33, para. 89 ("We conclude that support for a single residential connection will permit a household complete access to telecommunications and information services.").

²⁴⁰ See, e.g., Idaho Tel. Ass'n Comments at 9; OPASTCO Reply Comments at 21; Texas Statewide Tel. Coop. Comments at 11. Some commenters challenge the assumption that rates for second lines will rise if support is limited to single connections. See, e.g., AT&T Comments at 16 ("The costs of digging the trench or erecting the poles must be incurred fully in order to provide first-line service. There are few incremental costs to providing additional connections."); NASUCA Reply Comments at 14-15 ("Given the architecture of both wireline and wireless facilities, it is very likely that the cost of subsequent connections by either type of provider is much lower than the initial connection. Second lines provided by a single firm to a single household or business tend to be more profitable than the initial line. . . . Therefore, second lines may be provided at an affordable price in rural areas even without support, obviating concerns about increases to the price of second lines."); see also GCI Comments at 68-69 ("The vast majority of multiple connections provided today – the overwhelming bulk of the 148 million CMRS handsets – are not subsidized. . . . Moreover, studies have shown little if any difference in pricing between rural and urban markets.").

²⁴¹ See OPASTCO Comments at 6 ("many rural [incumbent] LECs provide DSL services, which provide a substitute for the second line a customer may have purchased to use for dial-up Internet access."). Commission data indicate that most asymmetric DSL connections are provided by LECs, which generally provision the service over the same line as their voice service. See Industry Analysis and Technology Division, Wireline Competition Bureau, *High-Speed Services for Internet Access: Status as of December 31, 2002* at Tbl. 5 (rel. June 10, 2003), available at www.fcc.gov/wcb/stats (high-speed asymmetric DSL technologies in service increased by 27% during the second half of 2002, from 5.1 million to 6.5 million lines).

²⁴² See, e.g., Western Wireless Comments at 10-11, Attachment B at 3-7.

²⁴³ See AT&T Comments at 10-11 ("if wireless functionality were added to the characteristics of a supported service in Section 54.101(a), non-wireless carriers (including [incumbent] LECs' wireline operations) could no longer be ETCs because they would not be able to provide a component of the supported services.").

²⁴⁴ See generally *Facilitating the Provision of Spectrum-Based Services to Rural Areas and Promoting Opportunities for Rural Telephone Companies to Provide Spectrum-Based Services*, Notice of Inquiry, WT Docket No. 02-381, 17 FCC Rcd 25554 (2003).

95. We also believe that supporting a single connection would fulfill the statutory principles of sufficiency and predictability.²⁴⁵ The Joint Board and the Commission have defined sufficiency as enough support to achieve relevant universal service goals without unnecessarily burdening all consumers for the benefit of support beneficiaries.²⁴⁶ The Fifth Circuit similarly noted that excessive funding may violate the sufficiency requirements of the Act, because excess support may detract from universal service by causing unnecessary increases in rates, thereby pricing some consumers out of the market.²⁴⁷ Supporting multiple connections for multiple networks is not necessary to achieve reasonably comparable access in rural areas, and creates a potential for fund growth that threatens the sustainability of the universal service fund.²⁴⁸ Accordingly, supporting primary connections better fulfills the sufficiency requirements of the Act.

96. Furthermore, contrary to the arguments of some commenters, the sufficiency and predictability principles do not provide that cost recovery should be guaranteed for particular carriers. OPASTCO, for example, argues that “[i]f rural ILECs are uncertain that they will be able to recover their network costs due to a primary connection support restriction, the incentive to continue investing in infrastructure will be inhibited. As a result, rural consumers’ access to high-quality services that are reasonably comparable to those offered in urban areas will be jeopardized.”²⁴⁹ Notably, no rural carrier would lose any high-cost support under our recommended approach unless a competitive ETC captures primary connections from the rural carrier following competitive ETC entry.²⁵⁰ But even if a rural carrier were to lose support in the future, that would not be inconsistent with sufficiency or predictability. The Fifth Circuit explained that “[t]he Act does *not* guarantee all local telephone service providers a sufficient return on investment; quite to the contrary, it is intended to introduce competition into the market. . . . The Act only promises universal service, and that is a goal that requires sufficient funding of *customers*, not *providers*.”²⁵¹ Congress clearly envisioned the presence of competitive ETCs in some areas served by rural carriers, provided a state makes the threshold determination that designating a competitive ETC is in the public interest.²⁵² The Act does not require or encourage supporting multiple connections for multiple networks, however. Supporting a single connection may not ensure sufficient funding of every ETC, but it would provide sufficient support for universal service.²⁵³

²⁴⁵ See 47 U.S.C. §§ 254(b)(5), 254(e).

²⁴⁶ *Tenth Circuit Remand Order*, FCC 03-239 at paras. 36-37 (“We also agree with the Joint Board that the principle of sufficiency encompasses the idea that the amount of support should be only as large as necessary to achieve the relevant statutory goal. Because support is ultimately recovered from customers, collecting more support than is necessary to benefit certain customers would needlessly burden all customers.”); see also *Federal-State Joint Board on Universal Service*, Second Recommended Decision, CC Docket No. 96-45, 13 FCC Rcd 24744, 24746, para. 3 (Jt. Bd. 1998) (*Second Recommended Decision*).

²⁴⁷ *Alenco v. FCC*, 201 F.3d at 620.

²⁴⁸ See *infra* paras. 98-99.

²⁴⁹ OPASTCO Reply Comments at 20.

²⁵⁰ See *infra* paras. 103-107. We note, however, that one proposal discussed below would “hold-harmless” incumbent carriers from any loss of universal service support. See *infra* para. 106.

²⁵¹ *Alenco v. FCC*, 201 F.3d at 620; see also *id.* at 623 (“the Commission reasonably construed the predictability principle to require only predictable *rules* that govern distribution of the subsidies, and not to require predictable *funding amounts*. Indeed, to construe the predictability principle to require the latter would amount to protection from competition and thereby would run contrary to one of the primary purposes of the Act.”).

²⁵² See 47 U.S.C. §§ 214(e)(1), (2). As discussed in Section II above, we recommend establishing rigorous and fact-intensive guidelines for public interest determinations required in ETC applications.

²⁵³ See *Alenco v. FCC*, 201 F.3d at 620 (“So long as there is sufficient and competitively-neutral funding to enable all customers to receive basic telecommunications services, the FCC has satisfied the Act and is not further required (continued....)

97. Although we do not believe that the federal support mechanism should continue to support multiple connections, we believe that states have the flexibility to establish their own support mechanisms for multiple connections, mobility, or other functionalities not supported at the federal level. Section 254(f) makes clear that states “may adopt regulations not inconsistent with the Commission’s rules to preserve and advance universal service” and that a state may “provide for additional definitions and standards” so long as those supplements do not rely on or burden the federal support mechanisms.²⁵⁴ Although such state support would go beyond the scope of federal high-cost support, we do not believe that such supplementary state funding would “rely on or burden Federal universal service support mechanisms” in contravention of section 254(f) of the Act.

2. Supporting a Single Connection Is Necessary to Protect Fund Sustainability

98. Continued support of multiple connections for multiple networks in rural and high-cost areas threatens fund sustainability. Currently, the support flowing to a high-cost area increases automatically when a competitive ETC is designated, according to the number of connections it serves.²⁵⁵ Competitive ETCs now receive a small fraction of total high-cost support, but their support has increased dramatically over the past few years.²⁵⁶ Much of this growth represents supported wireless connections that supplement, rather than replace, wireline service.²⁵⁷ Our examination of the record reveals a potential for uncontrolled growth as more and more competitive ETCs are designated in rural and high-cost areas.²⁵⁸ This potential is compounded by the calculation of support under the current rules.²⁵⁹ The Commission

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to ensure sufficient funding of every local telephone provider as well.”). Congress thought that competition and new technologies would reduce, not increase, the overall need for universal service support by lowering costs. *See* S. Rep. No. 23, 104th Cong., 1st Sess. 26 (“The Committee expects that competition and new technologies will greatly reduce the actual cost of providing universal service over time, thus reducing or eliminating the need for universal service support mechanisms as actual costs drop to a level that is at or below the affordable rate for such service in an area . . .”) (cited in *Tenth Circuit Remand Order*, FCC 03-249 at para. 77 n.296).

²⁵⁴ 47 U.S.C. § 254(f).

²⁵⁵ *See* NASUCA Comments at 5 (current rules “allow each new competitive entrant to impose incremental costs on all existing telecommunications customers”).

²⁵⁶ Based on USAC data, 2 competitive ETCs received just over \$500,000 in high-cost support in 1999, 4 competitive ETCs received \$1.5 million in 2000, 25 competitive ETCs received \$17 million in 2001, and 64 competitive ETCs received \$47 million in 2002. In 2003, 109 competitive ETCs received approximately \$131.5 million in high-cost support. Based on USAC quarterly projections, support for competitive ETCs will increase from \$62.9 million in the fourth quarter of 2003, to \$111.5 million in the second quarter of 2004, an increase of 77%. *See* Federal Universal Service Support Mechanisms Fund Size Projections and Contribution Base for the Second Quarter 2004, Appendix HC 18-21 (Universal Service Administrative Company, Jan. 31, 2004). We note that USAC quarterly projections include ETC applicants that have filed line count data with USAC, but are not yet designated as ETCs.

²⁵⁷ One study estimates that 3 to 5 percent of wireless customers use their wireless phones as their only phone. *See Implementation of Section 6002(B) of the Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Radio Services, Seventh Report*, 17 FCC Rcd 12985, 12989-90, para. 33 (*Seventh Annual CMRS Report*). *See also* AT&T Comments at 6-7; Sprint Comments at 7-8. There also is evidence in the record reflecting that some customers are replacing wireline phone usage with wireless service, and relying on wireless as their “primary” service. *See* OPASTCO Comments at 5; Smith Bagley Comments at 7; Texas Statewide Tel. Comments at 3; Western Wireless Comments, Attachment B at 5-6, Attachment C at 1-7.

²⁵⁸ *See, e.g.*, Independent Tel. & Telecomms. Alliance Reply Comments at 2-3; NASUCA Comments at 1-3; NTCA Comments at 10; OPASTCO Comments at 9-11. *See supra* note 183.

²⁵⁹ *See, e.g.*, AT&T Comments at 20-21 (“as a [competitive] ETC enters and takes lines from an [incumbent] LEC, total High Cost support to the study area increases because the [incumbent] LEC’s support does not fall to offset the
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declined to adopt the Joint Board's recommendation to limit support to single connections in 1997, based largely on its expectation that a forward-looking support methodology could be implemented for all incumbent LECs as early as January 1, 2001.²⁶⁰ Support for rural carriers likely will continue to be based on embedded costs at least until mid-2006, however.²⁶¹ We believe that the Commission should no longer defer limiting the scope of high-cost support. By limiting fund growth due to competitive ETC entry in rural and high-cost areas, our recommended approach would protect fund sustainability. High-cost support would increase with primary connection growth, rather than with growth in the total number of connections provided by both incumbent and competitive ETCs.

99. We reject arguments that supporting a single connection is not an effective means to slow fund growth because competitive ETCs receive a small percentage of total high-cost support and most fund growth over the past few years is attributable to support increases received by incumbent LECs.²⁶² The total amount of support received by competitive ETCs, for what appear to be supplemental connections for many subscribers, has increased substantially over the past few years. We believe that further growth due to supporting multiple connections presents a significant threat to fund sustainability. Our recommended approach addresses this concern directly in a manner that is consistent with statutory goals. To the extent that increases in high-cost funding for incumbent LECs present additional fund sustainability concerns, we expect to address those concerns in conjunction with our reexamination of the basis of support for all ETCs.²⁶³

3. Supporting a Single Connection Would Send More Appropriate Entry Signals and Would Be Competitively Neutral

100. Supporting a single point of access would send more appropriate entry signals in rural and high-cost areas. Some commenters argue that carriers increasingly are seeking ETC designation based on perverse incentives created by the current rules.²⁶⁴ Our recommended approach would not artificially encourage entry by competitive ETCs in areas where a rational business case cannot be made absent assumptions of support for *all* connections. Competitive ETCs instead would have incentives to enter rural and high-cost areas only where doing so makes rational business sense under a model assuming incremental support only for subscribers captured from, or unserved by, the incumbent LEC. Furthermore, by preventing automatic support of multiple connections, supporting a single point of access would address alleged incentives under the current rules for states to designate additional ETCs to attract more universal service funding.²⁶⁵

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[competitive] ETC's support. . . . The amount of support increases to even higher levels because there is a subsequent up-tick in [competitive] ETC support based on the [incumbent] LEC's now-increased effective per-line support."); *see also Rural Task Force Order*, 16 FCC Rcd at 11294-95, para. 125.

²⁶⁰ *First Universal Service Report and Order*, 12 FCC Rcd at 8829-30, paras. 95-96. *See also supra* paras. 90-91.

²⁶¹ *See Rural Task Force Order*, 16 FCC Rcd at 11246, 11248-49, paras. 1, 8-11.

²⁶² *See, e.g.*, Centennial Reply Comments at 2-3; CTIA Reply Comments at 2-4; Nextel Comments at 2, 6-8.

²⁶³ *See infra* paras. 125-128.

²⁶⁴ *See, e.g.*, ACS-F Comments at 7, 12-13; AT&T Comments at 22; GCI Comments at 41-43; OPASTCO Comments at 9-11.

²⁶⁵ *See, e.g.*, NASUCA Comments at 8-9 ("Under current rules, states have something of a conflict of interest. That is, here may be a bias toward granting of ETC status because, when new ETCs are created, more federal dollars flow into the state. Conversely, there is a disincentive for states to ensure that the public interest is fulfilled on a national basis because the benefit of additional federal funds may outweigh state regulators' concerns about the sustainability of the federal program.").

101. Supporting a single connection also would be competitively neutral.²⁶⁶ Support would be available to all ETCs for providing primary connections. To the extent that a competitive ETC replaced an incumbent ETC as the primary connection provider, the competitive ETC would receive support for providing the connection.²⁶⁷ In addition, rural carriers would no longer be insulated from the effects of universal service competition, because they would lose per-line support to the extent that they lose primary connections.²⁶⁸ Our recommended approach also would prevent upward spirals in per-line support amounts as a result of loss of lines by incumbent carriers, an unfortunate effect of the current rules that commenters argue creates potential windfalls for competitive ETCs.²⁶⁹

102. We disagree with commenters who argue that limiting support to a single connection would unfairly advantage incumbent LECs because they preceded competitive ETCs in rural and high-cost areas.²⁷⁰ Under our recommended approach, consumers would be free to designate any ETC as "primary" based on the service attributes that it offers.²⁷¹ We also reject an alternative proposal from Western Wireless to cap total high-cost support in an area upon competitive ETC entry and allocate the support among ETCs based on market share, in lieu of limiting support to a single connection.²⁷² Western Wireless contends that its alternative proposal would contain fund growth due to competitive ETC entry, but would be more competitively neutral and less administratively burdensome than a primary-connection limitation.²⁷³ In our view, however, this measure would continue support of multiple connections for multiple networks, contrary to the provisions of the Act discussed above. It also could lead to sudden, major shifts in support in areas where a new competitive ETC already serves a significant number of connections.

²⁶⁶ See *First Universal Service Report and Order*, 12 FCC Rcd at 8801-02, paras. 46-48 (pursuant to section 254(b)(7), adopting the principle that federal support mechanisms should be competitively neutral, neither unfairly advantaging nor disadvantaging particular service providers or technologies).

²⁶⁷ See AT&T Comments at 15-16; NASUCA Comments at 6.

²⁶⁸ See GCI Comments at 38 ("In an unsubsidized market, an [incumbent] LEC loses all of the revenue associated with service to a customer when it loses that customer to a competitor. By contrast, in an area receiving high cost support, although the [incumbent] LEC loses the end user revenue associated with that customer, it *retains* the high cost support associated with the facilities that were formerly used to serve that customer, because its high cost support does not decline when it loses the line."); see also AT&T Comments at 15-16. We note, however, that if the Commission adopts the "hold-harmless" approach discussed below, incumbent carriers would not lose high-cost support upon capture of primary lines by a competitive ETC. See *infra* para. 106.

²⁶⁹ See *Rural Task Force Order*, 16 FCC Rcd at 11294-95, para. 125; AT&T Comments at 22 ("Over the long term, these revenue guarantees give [competitive] ETCs a windfall by increasing the amount of [competitive] ETC support per line as ILEC per-line support increases. This allows [competitive] ETCs to enjoy increased revenue per connection, without any work or ingenuity on their part."); see also OPASTCO Comments at 13-14 (arguing that competitive ETCs receive a windfall under the current rules).

²⁷⁰ See generally Western Wireless Reply Comments, Attachment B (arguing that any distinction based on which connection is the "first line" would operate to benefit incumbent LECs and would not be competitively neutral because being "first" should not provide a carrier with "regulatorily conferred advantages").

²⁷¹ In this regard, we note that Western Wireless cites studies indicating that "more and more consumers view their wireless phones as their 'primary' voice services" because of the service attributes offered by wireless carriers. Western Wireless Comments, Attachment J at 4; see *id.* at Attachment B at 4-6 (providing data to support contention that subscribers are "substituting wireless for traditional wireline service").

²⁷² See Western Wireless Comments at 18.

²⁷³ See Western Wireless Comments, Attachment J at 7-8.

4. Maintaining Sufficient Support for Rural Areas

103. We recommend that the Commission take steps to avoid or mitigate reductions in the amount of high-cost support flowing to rural areas as a result of implementing a primary-line restriction.

a. Restatement Proposal

104. One way the Commission might accomplish this end would be to restate total current support paid to a rural carrier in terms of first lines. Rural carriers are eligible for high-cost support based on total embedded costs averaged on a study-area level.²⁷⁴ The total amount of high-cost support flowing to an area served by a rural carrier could be restated in terms of support *per first line*, rather than support *per line*, without any effect on the amount of support received by the rural carrier at the time support is restated.²⁷⁵ Restating support is a method of limiting the scope of support in areas served by rural carriers without modifying the basis of support (that is, the methodology used to calculate support).²⁷⁶

b. Lump Sum Payment Proposal

105. Alternatively, rather than increase the amount of per-line support available in areas served by rural carriers by restating support in terms of first lines, the Commission could provide supplemental lump sum payments to avoid any immediate effects on rural carriers as a result of limiting the scope of support. Under this approach, a rural carrier would receive the same amount of high-cost support on a per-line basis as it did previously, but would receive such support only for primary lines. The rural carrier also would receive a lump sum payment to compensate for the loss of support associated with existing second lines. Thus, this interim lump sum proposal, like the restatement proposal described in the previous paragraph, would prevent support reductions in rural areas based on the termination of support for second lines; high-cost support would be reduced only with the future loss of primary lines *to competitors*. But unlike the restatement proposal, the lump sum payment alternative would not increase the amount of per-line support for incumbent carriers, and thus would not encourage competitive carriers to seek ETC status merely for arbitrage purposes.²⁷⁷ On the other hand, we recognize that making lump-sum payments available to incumbents, but not to competitive ETCs, could be inconsistent with the

²⁷⁴ See 47 C.F.R. §§ 36.601, *et seq.* (high-cost loop support), 54.301 (local switching support), 54.303 (long term support), 54.901, *et seq.* (interstate common line support). Interstate access support also is available to rural carriers subject to price cap regulation of their interstate access rates. See 47 C.F.R. § 54.801, *et seq.* The Joint Board does not recommend limiting the scope of interstate access support at this time, because the interstate access support methodology prevents support increases due to competitive ETC entry. See AT&T Comments at 13 ("Because [interstate access support] is subject to a hard cap, it cannot be the source of uncontrolled High Cost Support growth.").

²⁷⁵ See AT&T Comments at 13.

²⁷⁶ As discussed below, we recommend that the Joint Board and the Commission consider possible modifications to the basis of support for all ETCs when they undertake the "comprehensive review of the high cost support mechanisms for rural and non-rural carriers as a whole to ensure that both mechanisms function efficiently and in a coordinated fashion" in the Rural/Non-Rural Review proceeding. Our recommendations do not impact or prejudice anything that the Joint Board and Commission may do in the future in examining the basis of support for all ETCs in all areas.

²⁷⁷ Several commenters argue that providing support to competitive carriers based on the incumbent LEC's costs creates arbitrage opportunities, because competitive carriers generally have lower costs. See *e.g.*, Alaska Tel. Ass'n Reply Comments at 18-19; CenturyTel Comments at 32-39; South Dakota Telecomms. Ass'n Reply Comments 4-6. To the extent this problem exists in some areas, increasing the amount of per-line support available to competitive carriers would exacerbate it.

principle of competitive neutrality.²⁷⁸

c. “Hold Harmless” Proposal

106. We also seek comment on a different alternative designed to maintain support for rural areas that does not encourage competitive carriers to seek ETC status merely for arbitrage purposes. Under this proposal, per line support available to competitive ETCs would freeze upon competitive entry. Competitive ETCs would only be able to obtain USF support for customers who designated their service as the primary line. We recognize that many parties contend that a per-line approach would jeopardize the sufficiency of support distributed to incumbent carriers. Such parties note that incumbent LECs have made substantial investments in infrastructure in reliance on such support. This proposal would not cap per-line support for incumbent carriers and would thus “hold harmless” incumbent carriers from the loss of universal service support.

107. We recommend that the Commission seek comment on the relative pros and cons of the restatement, the lump sum and hold harmless proposals. Leaving aside the question of which of these approaches has the most merit, we believe that if the Commission implements a primary-line restriction, it must adopt some means of preventing or mitigating reductions in the support available to rural carriers. The Joint Board and the Commission consistently have recognized the importance of a cautious approach to universal service reform in areas served by rural carriers, in light of their size, diversity, and regulatory history.²⁷⁹ Restating support or implementing the lump sum or hold harmless proposal would avoid any immediate effects on rural carriers as a result of limiting the scope of support, by placing them in the same total support position as they were in beforehand.²⁸⁰ In other words, a rural carrier would not be required to forego any of the support that it received before implementation of the primary-line restriction. Its support would be reduced in the future only to the extent that a competitive ETC captures primary lines from the rural carrier (except under the hold harmless proposal). Rural carriers also would forego future support increases associated with new, non-primary lines.²⁸¹ Restating support, providing a lump sum payment, or adopting a hold-harmless proposal will ensure that the transition to supporting basic access is not unduly disruptive in areas served by rural carriers.²⁸² We also recommend that the Commission seek comment on whether to restate support, provide lump sum payments or hold-harmless

²⁷⁸ We recommend that the Commission seek comment on whether to phase out the lump sum available to incumbent carriers, and, if so, over what time period.

²⁷⁹ See, e.g., *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Federal-State Joint Board on Universal Service, *Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, Prescribing the Authorized Rate of Return From Interstate Services of Local Exchange Carriers*, Second Report and Order and Further Notice of Proposed Rulemaking in CC Docket No. 00-256, Fifteenth Report and Order in CC Docket No. 96-45, Report and Order in CC Docket No. 98-77, Report and Order in CC Docket 98-166, 16 FCC Rcd 19613, 19620, 19668-69, paras. 12, 130-31 (2001) (*MAG Order*), *recons. pending*; *Rural Task Force Order*, 16 FCC Rcd at 11247, paras. 4-5.

²⁸⁰ For example, if an incumbent rural ETC receives \$10,000 in high-cost support based on its embedded costs for that study area, and provides supported services to 9,000 first lines and 1,000 additional lines, it receives high-cost support that equates to \$1.00 per line under the current rules. Under our recommended approach, that incumbent rural ETC would continue to receive a total of \$10,000 in high-cost support based on its embedded costs, but restating its support in terms of first lines would translate into \$1.11 effective per-first line support.

²⁸¹ We believe that such increases likely would be minimal due to trends such as the provision of voice and data services over a single digital subscriber line. See OPASTCO Comments at 6-7. Both rural carriers and competitive ETCs would be eligible for additional support for primary service to new customers previously unserved by any ETC. See NASUCA Comments at 6.

²⁸² See e.g., NASUCA Reply Comments at 25-26 (asserting that rebasing “will reduce the impact on the smaller rural incumbent LECs” of a single-line limitation).

support in areas served by non-rural carriers.²⁸³

5. Cap on Per-Line Support Upon Competitive Entry

108. In conjunction with the measures discussed above, we recommend that high-cost support in areas served by rural carriers be capped on a per-primary line basis when a competitive ETC is present or when a competitive ETC enters the market and be adjusted annually by an index factor. This recommendation is a modified version of a Rural Task Force proposal.²⁸⁴ Under our recommended approach, the total support flowing to a rural carrier (including high-cost loop support, local switching support, long term support, and interstate common line support²⁸⁵) would be capped on a per-primary line basis upon competitive entry. Thereafter, per-primary line support would be adjusted annually based on an index factor, rather than changes in the rural carrier's embedded costs. We also recommend that the Commission seek comment on the alternative approach of capping per-primary line support available to competitive ETCs upon competitive entry, consistent with the "hold-harmless" proposal discussed above.²⁸⁶

109. Capping per-primary line support in areas served by rural carriers is necessary to implement a primary-line limitation and to prevent an upward spiral in support due to capture of primary connections by competitive ETCs. As we have stated, the high-cost universal service mechanisms calculate support for rural carriers based on total embedded costs averaged on a study-area basis. Under these mechanisms, a rural carrier's per-primary line support automatically increases as its total embedded costs are spread over fewer lines.²⁸⁷ This has several implications for purposes of a primary-connection limitation. First, absent a per-primary line cap, a rural carrier would continue to receive support for new lines served—regardless of whether such lines provide primary connectivity—because any costs associated with the new connections would increase the rural carrier's total embedded costs and, therefore, the per-line support associated with the primary lines it serves. Likewise, a rural carrier would not lose support if it loses primary connections to a competitive ETC. Thus, the absence of a per-line cap would obviate the effect of a single-connection limitation. Moreover, fund size could grow significantly if rural carriers lose primary connections to competitive ETCs, because rural carriers would continue to receive the same total support, but the per-line support amounts available to both the incumbent LEC and competitive ETCs would increase as rural carriers' per-line costs were spread over fewer primary lines.²⁸⁸

110. We recognize that the Commission declined to cap per-line support in the *Rural Task Force Order*.²⁸⁹ Nevertheless, we believe that the Commission should adopt a modified version of the Rural Task Force's proposal at this time. As discussed above, support for competitive ETCs has

²⁸³ We also recommend that the Commission seek comment on whether transitional measures should be adopted for support paid to competitive ETCs operating as of the release date of this Recommended Decision. See *infra* para. 118.

²⁸⁴ See *Rural Task Force Order*, 16 FCC Rcd at 11293, para. 120; see also *supra* para. 92.

²⁸⁵ See *supra*, para. 92, n.158. We, however, recommend a broader cap on per-line support. See AT&T Comments at 23 (advocating a cap on high-cost loop support (HCLS), local switching support (LSS), long-term support (LTS), and interstate common line support (ICLS)).

²⁸⁶ See *supra* para. 106.

²⁸⁷ See *Rural Task Force Order*, 16 FCC Rcd at 11294-95, para. 125; see also AT&T Comments at 17-18 ("an [incumbent] LEC will only lose support under HCLS, LSS and ICLS to the extent that its study areas costs decline, irrespective of the number of lines served.").

²⁸⁸ See *Rural Task Force Order*, 16 FCC Rcd at 11294-95, para. 125; AT&T Reply Comments at 17-18; GCI Comments at 36-38.

²⁸⁹ See *Rural Task Force Order*, 16 FCC Rcd at 11294-97, paras. 123-130; see also *supra*, para. 92.

increased dramatically since 2001, and the danger of excessive fund growth that the Commission recognized at the time of the *Rural Task Force Order* is now clear and present.²⁹⁰ In addition, the Commission viewed the Rural Task Force proposal as having a relatively narrow purpose—to limit fund growth due to capture of connections by competitive ETCs²⁹¹—whereas our recommendations have the broad purpose of limiting the scope of high-cost support to primary connections. Furthermore, the danger of an upward spiral in support would be exacerbated because, to the extent that a competitive ETC captures primary connections, there would be fewer supported lines over which to spread a rural carriers' increased per-line costs.

111. We recommend that the Commission further develop the record on what index factor should be used to adjust capped per-line support each year. The Rural Task Force originally recommended the rural growth factor, which is equal to the sum of annual changes in the total number of lines served by rural carriers and the Gross Domestic Product-Chained Price Index (GDP-CPI), an inflation measure.²⁹² Alternatively, a modified rural growth factor that reflects annual changes in the total number of *primary* lines served by rural carriers might be appropriate. The Commission also should consider using the GDP-CPI alone. In this regard, the Commission noted in the *Rural Task Force Order* that because the rural growth factor includes annual rural line growth, "its application to individual lines receiving frozen support would result in double counting of line growth."²⁹³ Some commenters express similar concerns.²⁹⁴

6. Administrative Issues

112. We recommend that the Commission seek comment on how best to implement our recommended approach for supporting primary connections. Opponents raise various administrative concerns regarding a primary-connection limitation.²⁹⁵ On the other hand, proponents argue that limiting the scope of high-cost support is administratively feasible, and that the burdens would be small compared to the potential benefits.²⁹⁶ We reject arguments that a primary-connection limitation is inherently unworkable. As NASUCA points out, rules distinguishing between primary and other connections are not unprecedented, and the Commission has successfully implemented regulatory initiatives involving consumer choice.²⁹⁷ Nevertheless, we recognize that limiting the scope of high-cost support presents

²⁹⁰ See *supra* para. 98; *Rural Task Force Order*, 16 FCC Rcd at 11326, para. 209.

²⁹¹ See *Rural Task Force Order*, 16 FCC Rcd at 11294, para. 123 ("the purpose of this proposal is to prevent excessive fund growth in the universal service fund as a result of an incumbent carrier's loss of lines to a competitive [ETC]"). The Commission concluded that the likelihood of such growth occurring in the near future was speculative because, among other things, it would occur "only if a competitive [ETC] captures subscriber lines from an incumbent, not if it adds new lines." *Id.* at 11295-96, para. 126.

²⁹² See *Rural Task Force Order*, 16 FCC Rcd at 11266, para. 48.

²⁹³ *Id.* at 11295, para. 126.

²⁹⁴ See AT&T Comments at 23 n.57.

²⁹⁵ Opponents argue, among other things, that limiting the scope of high-cost support would require complex new rules to define "primary" lines, require costly tracking of primary lines, give rise to consumer gaming and a new type of carrier "slamming," and intrude on consumer privacy. See, e.g., Alabama Rural LECs Reply Comments at 9; Centennial Reply Comments at 12; Fred Williamson and Assocs. Comments at 26-27.

²⁹⁶ See, e.g., AT&T Reply Comments at 12-13; GCI Comments at 69; NASUCA Comments at 6-7; see also NASUCA Reply Comments at 13 ("None of the commenters' concerns appear to be without a readily available remedy.").

²⁹⁷ NASUCA Comments at 7 (asserting that LECs are currently required to distinguish between primary and other lines for assessing subscriber line charges (SLCs) and allowing Lifeline support, and noting that "[w]hen equal access and intraLATA presubscription began, every customer had to make new choices that were more complicated (continued....)

administrative challenges. The present record does not allow us to resolve these issues. We recommend, therefore, that the Commission further develop the record on how to implement support for primary connections. Our recommendations are conditioned on the Commission's ability to develop competitively neutral rules and procedures that do not create undue administrative burdens.

113. In particular, we recommend that the Commission further develop the record on proposals to allow consumers with more than one connection to designate an ETC's service as "primary."²⁹⁸ We believe that this is a promising approach because it would allow consumers—the intended beneficiaries of universal service²⁹⁹—to decide whether an ETC's service is "truly a substitute for basic universal service."³⁰⁰ Such proposals also have the merit of competitive neutrality, as consumers would be free to designate a primary ETC based on the service attributes that the ETC offers. In addition, they may avoid the need for complex and possibly artificial distinctions between primary and other connections by placing choice in the hands of consumers. We are not persuaded by arguments that competition for primary designations would disserve the public interest by diverting ETCs' resources from infrastructure investment to marketing and promotion.³⁰¹ Where a state makes the threshold determination under the Act that universal service competition in a rural area would serve the public interest,³⁰² we expect that increased competition and choice will encourage investment and benefit consumers.

114. We also recommend that the Commission further develop the record on rate issues associated with supporting primary connections. Some commenters argue that limiting the scope of high-cost support would require local rate increases or pricing flexibility for second connections, and create ratemaking complexities for states.³⁰³ Others argue that supporting a single point of access need not mean different end-user rates for primary and other connections.³⁰⁴ AT&T argues that rate-of-return

(...continued from previous page)

than a selection of what firm provides the primary line."'). Opponents argue that difficulties in administering a primary/non-primary line distinction for price cap carriers' SLC rates would be exacerbated for small rural carriers in a multi-carrier environment. *See e.g.*, OPASTCO Comments at 35-37.

²⁹⁸ *See* NASUCA Comments at 6 ("The primary line should be designated by each customer with more than one line, and carriers should be free to compete for the designation as 'primary.' The Commission should allow a reasonable transition period within which consumers could exercise their choice if they have more than one line or if they are served by more than one ETC. However, the Commission will have to devise a system to deal with customers who fail to indicate a choice by the end of the transition period. One way to determine the primary line would be to designate the initial [incumbent] LEC line as the default primary connection. Another alternative is to require a ballot to be submitted by every customer with multiple connections, which entails more administrative burden. While the default assumption would be that a single address represents a single household, there should be flexibility to allow a customer to rebut that presumption by submitting contrary information to the carrier."); *see also* Western Wireless Comments, Attachment J at 6-7 (advocating use of vouchers or "phone stamps" as a means of implementing a primary connection restriction with consumer choice)..

²⁹⁹ *Alenco v. FCC*, 201 F.3d at 621 ("The purpose of universal service is to benefit the customer, not the carrier.").

³⁰⁰ NASUCA Comments at 6.

³⁰¹ *See, e.g.*, Rural Cellular Ass'n/Alliance of Rural CMRS Carriers Comments, Exhibit 1 at 20; Letter from Karen Brinkman, Counsel for CenturyTel Inc., to Marlene Dortch, FCC, dated Dec. 18, 2003 (CenturyTel Dec. 18 *ex parte*)

³⁰² *See* 47 U.S.C. § 214(e)(2).

³⁰³ *See, e.g.*, OPASTCO Comments at 38-39; MUST Comments at 36; Townes et al. Comments at 8-9; *see also* AT&T Comments at 24-27; SBC Comments at 16-17.

³⁰⁴ *See* NASUCA Reply Comments at 10-11. NASUCA argues that carriers can charge averaged rates, and that states can provide support for secondary connections if they so choose. *See id.* at 13-14, 22-23.

carriers should be permitted to increase federal subscriber line charges on non-supported lines to recover any lost interstate common line revenues, although it maintains that such increases are unlikely.³⁰⁵ States will determine local rate issues in the intrastate ratemaking process, but further development of the record may assist states in addressing these issues.

7. Other Issues

115. We also recommend that the Commission further develop the record on the appropriate treatment of businesses with multiple connections, particularly small businesses, under our recommended approach.³⁰⁶ Historically, the Joint Board and Commission have concluded that universal service concerns are not as great for multi-line business customers.³⁰⁷ Some commenters, however, have raised concerns that limiting support to a single point of access provided for residential and business customers may discourage operation of businesses, particularly small businesses, in rural areas.³⁰⁸ Commenters have noted that rural economies are highly dependent on the presence of businesses to provide jobs and services.³⁰⁹ Restating support should address these concerns to a large extent by avoiding upward pressure on rates for all customers in rural areas.³¹⁰ Nevertheless, we believe that these concerns warrant careful consideration. One possible means to address such concerns with regard to small businesses is to allow high-cost support for some designated number of multiple connections for businesses, rather than restricting support to a single business connection.³¹¹

116. As the Commission develops the record in this proceeding, it also should consider the treatment of lines provided by unbundled network element (UNE)-based competitive ETCs under our recommended approach. Unlike loss of a customer to a facilities-based carrier, loss of a customer to a UNE-based provider does not eliminate the need to continue operating the incumbent's network for the benefit of that customer.³¹² UNE rates compensate incumbent LECs for the forward-looking economic costs of providing UNEs under the current rules.³¹³ Some commenters, however, argue that UNE rates do not compensate incumbents for their embedded costs of providing UNEs and that this disparity creates

³⁰⁵ See AT&T Comments at 24-27.

³⁰⁶ Under the Regulatory Flexibility Act, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act. See 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in the Small Business Act, 15 U.S.C. § 632). A "small business concern" is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration. 15 U.S.C. § 632.

³⁰⁷ See, e.g., *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges*, First Report and Order, CC Docket Nos. 96-262, 91-213, 95-72, 12 FCC Rcd 15982, 16005, paras. 58-60 (1997) (*Access Charge Reform Order*) (subsequent history omitted) (concluding that higher SLC caps were warranted for such users).

³⁰⁸ See e.g., Idaho Tel. Ass'n Comments at 9; OPASTCO Comments at 37-38; USTA Comments at 6; Washington Commission Comments at 15.

³⁰⁹ Washington Commission Comments at 15-16. See also OPASTCO Comments at 37.

³¹⁰ See *supra* para. 107. See also AT&T Comments at 12-16.

³¹¹ In Texas, for example, lines eligible for intrastate support are currently limited to all flat rate residential lines and the first five flat rate single-line business lines at the business customer's location within the state of Texas. See Texas Commission Comments at 10.

³¹² See e.g., ACS-F Reply Comments 9-12.

³¹³ 47 C.F.R. § 54.307(a)(2). See also GCI Comments at 58-61 (noting that "the Commission rejected embedded costs as a measure of the [incumbent] LEC's true economic costs for the purposes of setting UNE prices based on costs").

arbitrage opportunities.³¹⁴ Under the current universal service rules, incumbent LECs do not normally receive high-cost support when they lose lines to UNE-based competitive ETCs unless the support exceeds the UNE price.³¹⁵ We believe that these matters warrant consideration by the Commission.

117. More generally, we encourage the Commission to seek comment on the impact of our primary connection proposal on investment in rural areas. Opponents of this proposal contend that it would undermine investment by incumbent LECs and competitors.³¹⁶ We do not expect such an outcome, but we urge the Commission to give this issue careful consideration.

118. Finally, we encourage the Commission to consider whether it should adopt transitional measures for support in areas where competitive ETCs are operating as of the release date of this Recommended Decision. We recognize that business plans may be contingent on support received under the current rules. Like restating per-line support for rural carriers, transitional measures for support received by competitive ETCs may be appropriate. Transitional measures also may be appropriate to avoid rapid shifts in support and provide all ETCs with time needed to adjust their business plans. One possible approach would be to establish a transitional period during which support for non-primary connections is phased down annually.³¹⁷ In addition, any shifts in support due to customer choice of a primary connection provider could be limited to a given percentage for all ETCs during the transition period.³¹⁸

VIII. BASIS OF SUPPORT

119. We decline to recommend that the Commission modify the basis of support in areas with multiple ETCs at this time, but we will continue to consider possible modifications to the basis of support in this proceeding. We recommend that the Joint Board and the Commission continue to consider possible modifications to the basis of support in a broader context. Specifically, we recommend that the Joint Board and the Commission consider possible modifications to the basis of support for all ETCs when they undertake the "comprehensive review of the high-cost support mechanisms for rural and non-rural carriers as a whole to ensure that both mechanisms function efficiently and in a coordinated fashion" in the Rural/Non-Rural Review proceeding.³¹⁹ Examining the basis of support in areas with multiple ETCs in conjunction with review of the rural and non-rural mechanisms would allow the Joint Board and the Commission to craft a more comprehensive approach and avoid the perils of piecemeal decision-making. For the present, the Joint Board will continue its review of the methodology for calculating support for ETCs in areas with multiple ETCs.

A. Background

120. In the *First Universal Service Report and Order*, the Commission determined that federal high-cost support for all eligible carriers eventually should be based on the forward-looking economic

³¹⁴ See ACS-F Comments at 13-17; NTCA Comments at 13; OPASTCO Comments at 18-22.

³¹⁵ See 47 C.F.R. § 54.307(a)(2).

³¹⁶ See, e.g., Idaho Tel. Ass'n Comments at 9; OPASTCO Comments at 31-33; Texas Statewide Tel. Coop. Comments at 11.

³¹⁷ See e.g., *Federal-State Joint Board on Universal Service*, Thirteenth Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-45, 15 FCC Rcd 24422 (2000) (*Thirteenth Report and Order*) (phasing down interim hold-harmless support for non-rural carriers).

³¹⁸ See NASUCA Reply Comments at 21-33; SBC Comments at 14-16.

³¹⁹ *Rural Task Force Order*, 16 FCC Rcd at 11310, para. 169; see also *Tenth Circuit Remand Order*, FCC 03-249 at para. 25.

cost of constructing and operating the network facilities and functions used to provide the supported services.³²⁰ The Commission agreed with the Joint Board that, “in the long run, forward-looking economic cost best approximates the costs that would be incurred by an efficient carrier in the market,”³²¹ and, therefore, the use of forward-looking economic cost as the basis for determining support will send the correct signals for entry, investment, and innovation.³²² The Commission concluded that “the 1996 Act’s mandate to foster competition in the provision of telecommunications services in all areas of the country and the principle of competitive neutrality compel [the Commission] to implement support mechanisms that will send accurate market signals to competitors.”³²³

121. Although the Commission generally concluded that federal high-cost support should be based on forward-looking economic costs rather than embedded costs, it agreed with the Joint Board that rural carriers should transition to support based on forward-looking costs at a later date than non-rural carriers.³²⁴ The Commission wanted to allow ample time for rural carriers to adjust to any changes in support calculations. In the meantime, rural carriers would receive support based on the existing embedded cost mechanisms, as modified in the *First Universal Service Report and Order*.³²⁵

122. In order not to discourage competition in high-cost areas, the Commission determined that an incumbent’s high-cost support should be portable to other eligible carriers prior to the transition to forward-looking economic cost mechanisms.³²⁶ The Commission found that the least burdensome way to administer the support mechanisms would be to calculate an incumbent LEC’s per-line support amount based on its embedded costs and provide this per-line amount to all ETCs serving customers within the service territory.³²⁷ The Commission recognized that a competitive ETC may have different costs than the incumbent LEC, but explained that competitive ETCs must comply with section 254(e) of the Act, and that section 214(e) requirements would prevent competitive ETCs from profiting by limiting service to low cost areas.³²⁸ In addition, the Commission determined that the alternative, requiring competitive ETCs to submit forward-looking cost studies without requiring the incumbent LEC’s support to be calculated in the same manner, could place either the incumbent LEC or the competitive ETC at a competitive disadvantage.³²⁹

123. In the *Rural Task Force Order*, the Commission further modified the embedded cost support mechanisms for rural carriers for a five-year period based on the recommendations of the Rural Task Force. The Commission stated its intention to refer to the Joint Board the issue of the appropriate rural mechanism to succeed the Rural Task Force plan.³³⁰ In the context of the Joint Board’s

³²⁰ See *First Universal Service Report and Order*, 12 FCC Rcd at 8899, para. 224; see also *First Recommended Decision*, 12 FCC Rcd at 230-32.

³²¹ *First Universal Service Report and Order*, 12 FCC Rcd at 8899, para. 224; see also *First Recommended Decision*, 12 FCC Rcd at 230, para. 270.

³²² See *First Universal Service Report and Order*, 12 FCC Rcd at 8899, para. 224.

³²³ *First Universal Service Report and Order*, 12 FCC Rcd at 8935, para. 292.

³²⁴ *Id.* at 8934-37, paras. 291-95.

³²⁵ *Id.* at 8937-45, paras. 297-313.

³²⁶ *Id.* at 8934, 8944, paras. 291, 311.

³²⁷ *Id.* at 8933, 8945, paras. 288, 313.

³²⁸ *Id.* at 8933, para. 289.

³²⁹ *Id.* at 8945, para. 313. It does not appear that the Commission considered the alternative of requiring competitive ETCs to submit *embedded* cost studies. This is not surprising given the emphasis in the *First Universal Service Report and Order* on eventually basing support for all carriers on forward-looking economic cost.

³³⁰ *Rural Task Force Order*, 16 FCC Rcd at 11310, para. 168.

consideration of an appropriate rural mechanism, the Commission stated that it anticipated "conducting a comprehensive review of high-cost support mechanisms for rural and non-rural carriers as a whole to ensure that both mechanisms function efficiently and in a coordinated fashion."³³¹ The Commission said that it would "use the transitional period during which a modified embedded cost mechanism is in place to develop a long-term universal service plan that better targets support to rural telephone companies serving the highest cost areas and recognizing the significant distinctions among rural carriers and between rural and non-rural carriers."³³² The Commission also said that it would include consideration of general issues related to excessive fund growth and competitive neutrality in that comprehensive review.³³³

124. In the *Referral Order*, the Commission asked the Joint Board to review the methodology for calculating support for ETCs in competitive study areas.³³⁴ The Commission noted that some groups have argued that basing a competitive ETC's support on the incumbent LEC's embedded costs provides a windfall and creates an unfair advantage for competitive ETCs with lower costs, whereas others have argued that the current rules are necessary for competitive neutrality and are the least administratively burdensome way to administer support.³³⁵ The Joint Board sought comment regarding the methodology for calculating support for ETCs in areas served by multiple ETCs.³³⁶ Among other things, the Joint Board sought comment on: whether the current rules promote efficient competition in high-cost areas and operate in a competitively neutral manner; whether the Commission should calculate support for a competitive ETC based on its own costs; whether the methodology used to calculate competitive ETC support should be the same as the methodology used to calculate support for the incumbent; and whether support in competitive areas should be based on the lowest-cost provider's costs, in order to promote efficiency.³³⁷

B. Discussion

125. We recommend that the Commission ask the Joint Board to continue to consider possible modifications to the basis for determining support for competitive ETCs in conjunction with review of the appropriate high-cost mechanism for rural carriers to succeed the five-year plan adopted in the Rural Task Force Order. The Commission recently reiterated its intention to ask the Joint Board "to conduct a comprehensive review of the high-cost support mechanism for rural and non-rural carriers as a whole to ensure that both mechanisms function efficiently in a coordinated fashion."³³⁸ Because the Commission anticipates that the Joint Board will conduct a comprehensive review of both rural and non-rural mechanisms in the context of our consideration of an appropriate rural mechanism, we recommend that the Joint Board be asked to consider the basis of support for all ETCs in all areas in the Rural/Non-Rural Review proceeding. For the present, the Joint Board will continue its review of the methodology for calculating support for ETCs in areas with multiple ETCs.³³⁹

³³¹ *Id.* at 11310, para. 169.

³³² *Id.*

³³³ *Id.*

³³⁴ *Referral Order*, 17 FCC Rcd at 22645-46, para. 7.

³³⁵ *Id.*

³³⁶ *Joint Board Portability-ETC Public Notice*, 18 FCC Rcd at 1948-51, paras. 15-23.

³³⁷ *Id.* at 1948-50, paras. 16, 18-19.

³³⁸ *Tenth Circuit Remand Order*, FCC 03-249 at para. 25.

³³⁹ *Referral Order*, 17 FCC Rcd at 22645, para. 7 (asking Joint Board "to review the methodology for calculating support for ETCs in competitive study areas.").

126. Considering the basis of support under the rural and non-rural mechanisms simultaneously would allow the Joint Board to craft a more comprehensive approach and avoid the perils of piecemeal decision-making. We anticipate that the Commission in the Rural/Non-Rural Review proceeding will ask us to simultaneously consider both the rural and non-rural support mechanisms and to develop recommendations regarding the possible harmonization of the divergent approaches (embedded costs vs. forward-looking costs).³⁴⁰ We believe that it would be appropriate to consider the basis of support in competitive areas in this broader context. Our approach to harmonizing the two mechanisms will necessarily influence our recommendations on the basis of support in competitive areas.³⁴¹

127. For areas served by rural carriers, we are concerned that funding a competitive ETC based on the incumbent LEC's embedded costs may not be the most economically rational method for calculating support. However, we do not yet have an adequate record to analyze and understand the consequences of recommending a change in the basis of support for areas served by rural carriers that face competition. We agree that universal service payments should not distort the development of nascent competitive markets. Universal service support should neither incent nor discourage competitive entry. We also believe that further work may be needed to decide if and how support should be adjusted to reflect differences in service obligations, service quality and functionality. While we do not have an adequate record at this time to determine how, and if, the current basis of support should be modified to achieve these goals, we are concerned about any potential negative consequences for rural markets. Therefore, we believe that further analysis should be conducted before potential changes are made. Rural carriers were put on notice that the Joint Board and Commission would begin reviewing the current mechanism that provides support to rural carriers based on their embedded costs before 2006. In the Rural/Non-Rural Review proceeding, we plan to consider methods for determining support to high cost areas. These methods should be competitively neutral, administratively simple and consistent with the Commission's goal of ensuring that the high-cost mechanisms function efficiently. We encourage all carriers that may be affected by this potential change to actively participate in the development of the record. We also emphasize that we have not yet determined whether it is appropriate to continue to maintain separate support mechanisms for rural and non-rural carriers.

128. We do not believe that delaying our consideration of the basis of support will undermine the sustainability of the universal service fund. Because the Commission determined that the Rural Task Force plan should remain in place until 2006, the Joint Board and the Commission have adequate time to conduct a comprehensive proceeding on the basis of support.³⁴² Moreover, if the Commission adopts the

³⁴⁰ In developing a long-term universal service plan, the Commission said that it intends "to consider all options, including the use of forward-looking costs, to determine appropriate support levels for both rural and non-rural carriers." *Rural Task Force Order*, 16 FCC Rcd at 11310, para. 170. The Commission also emphasized that the Act does not require separate rural and non-rural support mechanisms. *Id.* at 11310, para. 171 n.402. Although the Commission found that a distinct rural mechanism, based on embedded cost, was appropriate for the five-year period, it expressed its belief "that there may be significant problems inherent in indefinitely maintaining separate mechanisms based on different economic principles." *Id.* at 11311, para. 173.

³⁴¹ Many commenters agree that the basis of support for competitive ETCs is "inextricably linked" with broader issues in the Rural/Non-Rural Review proceeding. *See, e.g.,* Western Wireless Comments at 4 ("the issues raised to date in this proceeding are inextricably linked with the broader issues involved with the forthcoming 'comprehensive review of the high-cost support mechanisms for rural and non-rural carriers as a whole to ensure that both mechanisms function efficiently and in a coordinated fashion,' a process that the Commission has stated it intends to complete by 2006.").

³⁴² In the *Rural Task Force Order*, the Commission determined that the modified embedded cost mechanisms should remain in place to "provide certainty and stability for rural carriers for the next five years." *Rural Task Force Order*, 16 FCC Rcd at 11249, para. 11. *See also* Western Wireless Comments at 4 ("the industry remains in year two of a five-year plan for supporting universal service in rural [incumbent] LEC areas. The Commission found that the five-year duration of Rural Task Force ('RTF') plan, in which full portability of all explicit funding plays a critical role, was important to establish a stable and predictable environment for rural service providers.").

Joint Board's recommendations, discussed above, to adopt a primary-connection restriction and measures to ensure that ETC designations are appropriately rigorous, such steps should slow fund growth due to competitive ETC entry in the meantime. Accordingly, we recommend that the Commission refer to the Joint Board early this year the Rural/Non-Rural Review proceeding, including the consideration of the basis of support for all ETCs.

IX. OTHER ISSUES

A. Identification of Wireless Customer Location

1. Background

129. Currently, competitive ETCs that provide mobile wireless service are required to use the customer's billing address to identify the location of a mobile wireless customer within a disaggregation zone.³⁴³ In the *Rural Task Force Order*, the Commission concluded that this approach was reasonable and the most administratively simple solution to the problem of determining the location of a wireless customer for universal service purposes.³⁴⁴ The Commission recognized, however, that the use of a customer's address could allow arbitrage, such as "identifying a customer in a high-cost zone when service is primarily taken in a low-cost zone for the purpose of receiving a higher level of per-line support."³⁴⁵ The Commission stated that it would take appropriate enforcement action if an ETC were to engage in such arbitrage, and that it might revisit the use of a customer's billing address as more mobile wireless carriers are designated as eligible to receive support.³⁴⁶

130. The Commission declined to use the Mobile Telecommunications Sourcing Act (MTSA) definition of "place of primary use" to determine a mobile wireless customer's location.³⁴⁷ The MTSA, which was intended to address the difficulty in identifying the sites of a mobile telephone call for transactional tax purposes, sources all wireless calls and mobile telecommunications services to the "place of primary use."³⁴⁸ The place of primary use is defined as "the street address representative of where the customer's use of the mobile telecommunications service primarily occurs, which must be—(A) the residential street address or the primary business street address of the customer; and (B) within the licensed service area of the [customer's mobile telecommunications service provider]."³⁴⁹ In declining to adopt the MTSA definition to determine wireless customer location for universal service purposes, the Commission expressed concern that states might not have established databases pursuant to the Act, and that use of the MTSA definition might impose undue administrative burdens on mobile wireless ETCs.³⁵⁰

³⁴³ *Rural Task Force Order*, 16 FCC Rcd at 11314, para. 180.

³⁴⁴ *Id.* at 11314-15, paras. 180-181.

³⁴⁵ *Id.* at 11315-16, para. 183.

³⁴⁶ *Id.*

³⁴⁷ *Id.* at 11315, para. 182.

³⁴⁸ The MTSA gives states the option of providing mobile providers with a statewide database that designates the appropriate taxing jurisdiction for each street address in the state, including, to the extent practicable, multiple postal addresses applicable to one street location. If the state fails to provide such a database, the mobile provider may use an enhanced zip code system to assign each street address to a specific taxing jurisdiction. Under the MTSA, a mobile provider that uses a state-assigned database or an enhanced zip code system to assign addresses will be held harmless for any taxes that might otherwise be due as a result of erroneous assignment. Mobile Telecommunications Sourcing Act, 4 U.S.C. §§ 116-126.

³⁴⁹ *Id.*

³⁵⁰ *Rural Task Force Order*, 16 FCC Rcd 11315, para. 182.

131. Commenters allege that some ETCs may be engaged in the type of arbitrage that the Commission identified in the *Rural Task Force Order*, and state that the Commission should direct the Universal Service Administrative Company (USAC) to take measures to prevent abuse regarding the location of the connections of the wireless provider's customers.³⁵¹ A number of commenters also express a general concern that the billing address for a mobile wireless phone number has no relationship to where the customer actually uses the phone.³⁵² Other commenters advocate defining mobile wireless customer location in terms of the place of primary use, and offer different proposals for defining this concept, including the MTSA definition.³⁵³ The Texas Commission requires wireless ETCs to provide a wireless access unit (WAU) to determine the actual location of a connection for universal service purposes.³⁵⁴

132. Other commenters advocate the continued use of billing addresses to determine mobile wireless customer location.³⁵⁵ One commenter asserts that billing address is an accurate means to determine the location for high-cost support purposes,³⁵⁶ and others point out that line counts are publicly available and can be audited by USAC. BellSouth suggests that wireless ETCs be required to demonstrate that they provide a signal to a customer's billing address. BellSouth states that this demonstration could take the form of a customer certification that service at the billing address is available, working, and adequate.³⁵⁷

2. Discussion

133. The Joint Board recommends that the Commission further develop the record on defining mobile wireless customer location in terms of place of primary use for universal service purposes. The Joint Board believes that the place of primary use represents the preferred definition of wireless customer location for universal service purposes because it reflects whether a customer actually uses mobile wireless phone service as a primary connection in a high-cost area. Based on our examination of the present record, however, we cannot determine whether any of the definitions proposed by commenters, including the MTSA definition, are capable of being implemented in a competitively neutral manner that would not impose undue administrative burdens. Accordingly, the Joint Board recommends that the Commission further develop the record on this matter.

134. In particular, the Joint Board recommends that the Commission develop the record on the following issues: First, is the MTSA's place of primary use approach an efficient method to redefine the

³⁵¹ See OPASTCO Comments at 24-26, Reply Comments at 15-16. OPASTCO cites comments filed by the Washington Indep. Tel. Ass'n, USTA, and SBC to support the contention that the record documents the potential abuse of the rules that use a customer's billing address to identify the service location of a mobile wireless customer's service area.

³⁵² See, e.g., CenturyTel Comments at 35-36; Rural Indep. Competitive Alliance Comments at 19, 21.

³⁵³ See, e.g., Montana Telecomms. Ass'n Comments at 11-12; Washington Indep. Tel. Ass'n Comments at 14; Western Wireless Sept. 8 *ex parte*. Montana Telecomms. Ass'n and Western Wireless support use of the MTSA definition of place of primary use. Washington Indep. Tel. Ass'n recommends requiring a wireless carrier to certify that at least 50% of the originating calls on a wireless service originate in a cell site within the exchange for which the lie is designated to receive USF support.

³⁵⁴ Texas Commission Comments at 12. Wireless carriers report access lines in accordance with the actual location of the WAU that is utilized to provide the service.

³⁵⁵ Rural Cellular Ass'n/Alliance of Rural CMRS Carriers Comments at 26; Smith Bagley Comments at 13; Western Wireless Comments at 49-50.

³⁵⁶ Rural Cellular Ass'n/Alliance of Rural CMRS Carriers Comments at 26.

³⁵⁷ See BellSouth Comments at 2, Reply Comments at 5; see also GVNW Comments at 11, Reply Comments at 8-9.

location of mobile service lines? This may in part depend on the extent to which post office boxes are used to misrepresent customer locations. Second, should the use of a place of primary use-based definition be optional or mandatory? Third, what amount of fraudulent use of billing addresses is occurring today that use of a definition based on place of primary use would address? If place of primary use is adopted how should it work in conjunction with virtual NXX?

B. Accurate, Legible, and Consistent Maps

1. Background

135. Under the Commission's rules, a rural carrier electing to disaggregate and target high-cost support must submit to USAC "maps which precisely identify the boundaries of the designated disaggregation zones of support within the carrier's study area."³⁵⁸ In the *Rural Task Force Order*, the Commission explained that "the integrity and flow of information to competitors is central to ensuring that support is distributed in a competitively neutral manner."³⁵⁹ The Commission went on to state that, "in order to ensure portability and predictability in the delivery of support," it would require rural carriers to "submit to USAC maps in which the boundaries of the designated disaggregation zones of support are clearly specified."³⁶⁰ USAC was directed to make those maps available for public inspection by competitors and other interested parties.³⁶¹ Some commenters indicate that the maps filed by rural carriers pursuant to section 54.315(f)(1) and the information available through USAC are of varying quality and utility.³⁶² Others suggest that improved quality and reliability of maps submitted by incumbents would allow for better targeting of support.³⁶³

2. Discussion

136. We recommend that the Commission delegate authority to USAC to develop standards for the submission of any maps that ETCs are required to submit to USAC under the Commission's rules in a uniform, electronic format. We believe that the development of such standards would promote the integrity and flow of information to competitive ETCs by increasing the accuracy, consistency, and usefulness of maps submitted to USAC, and that as the universal service administrator USAC is the appropriate entity to develop such standards.

³⁵⁸ 47 C.F.R. § 54.315(f)(4).

³⁵⁹ *Rural Task Force Order*, 16 FCC Rcd at 11307-08, para. 161

³⁶⁰ *Id.*

³⁶¹ *Id.*

³⁶² See, e.g., USCC Comments at 17-18; Rural Indep. Competitive Alliance Comments at 27.

³⁶³ Rural Cellular Ass'n/Alliance of Rural CMRS Carriers Comments at 26 ("What will improve the ability to target subscribers is an FCC requirement that ILECs who disaggregate support submit accurate and legible cost zone maps in a consistent electronic format so that competitive ETCs are able to easily determine the appropriate cost zones for customers.").

X. RECOMMENDING CLAUSE

137. For the reasons discussed herein, the Federal-State Joint Board on Universal Service, pursuant to sections 254(a)(1) and 410(c) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 254(a)(1), 410(c), recommends that the Commission adopt recommendations set forth herein concerning the process for designation of eligible telecommunications carriers and the Commission's rules regarding high-cost universal service support.

FEDERAL COMMUNICATIONS COMMISSION

A handwritten signature in cursive script, reading "Marlene H. Dortch".

Marlene H. Dortch
Secretary